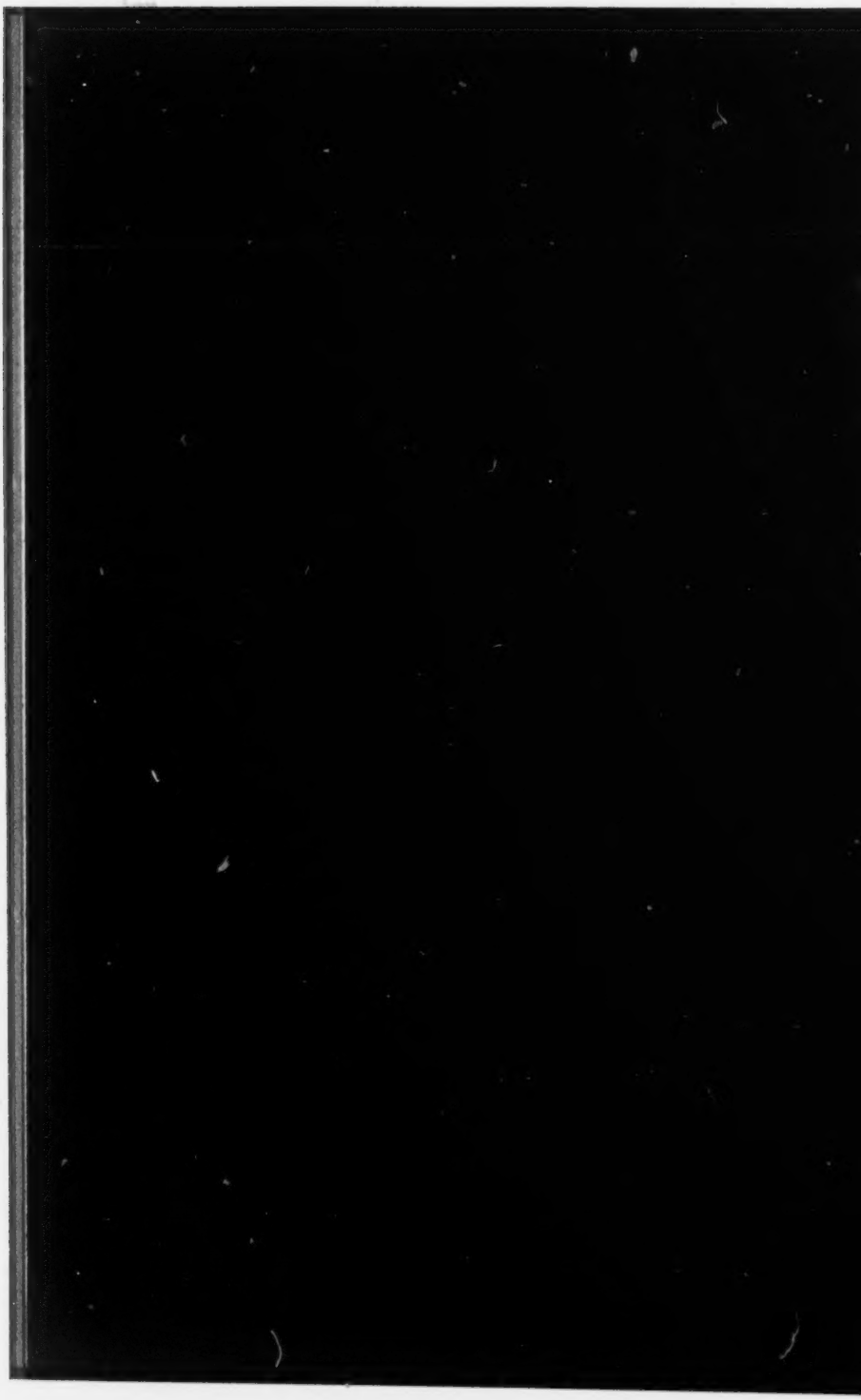

In the Supreme Court
OF THE
United States

OCTOBER TERM, 1943

No.

N. N. S. MATCOVICH,
Petitioner,

vs.

CLIFFORD C. ANGLIM, as Collector of Internal Revenue for the First District of California,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

PRELIMINARY MATTER.

The petition makes reference to the judgment below, states the jurisdictional grounds and states the facts, which statements are adopted.

SPECIFICATION OF ERRORS.

We believe that the Court erred as follows:

(1) The holding of the Ninth Circuit Court of Appeals that the case of *Griffith v. Commissioner,* 308 U. S. 355-358, overrides the license agreement in question where at no time was there any issue of fraud or claim made that the license agreement was drawn for the purpose of avoiding the tax in question, which holding is contrary to that in *Commissioner v. Falcon Co.,* 127 Fed. (2d) 277 (Fifth Circuit).

(2) The Court erred in holding that the state law was not controlling. It held that the employer-employee relationship should be determined according to the principles of common law. While it previously held in the case of *Childers v. Commissioner,* 80 Fed. (2d) 27-30, that the California law fixed the standard by which that relationship should be determined, the principles announced in the *Childers* case were not followed in the case at bar.

(3) That it erred in holding that the license agreement under the laws of the State of California was not conclusive on the origin and existence of the relationship to be a license and not an employment contract.

SUMMARY OF ARGUMENT.

(1) The rule announced in the case of *Griffith v. Commissioner,* 308 U. S. 355-358, to the effect "taxes cannot be escaped by anticipatory arrangements and contracts, however skillfully devised", should be lim-

ited to cases involving fraud or subterfuge. Some reason must be established before a contract can arbitrarily be set aside.

(2) Since the Circuit Court holds that the relationship of employer-employee should be fixed according to the standard of the common law and that there is no substantial difference between the common law and the California law, the conclusion that the state law is not controlling cannot be sustained. In addition, the Circuit Court in the case of *Childers v. Commissioner,* 129 Fed. (2d) 27-30, laid down the rule that under the similar circumstances that relationship was to be determined according to the California law.

(3) That according to the decisions of the Federal Courts, the license agreement should have been construed under the laws of the State of California.

ARGUMENT.

(1) THE NINTH CIRCUIT OF THE COURT OF APPEALS DIFFERS IN THE CONSTRUCTION OF THE RULE LAID DOWN IN GRIFFITH v. COMMISSIONER, 308 U. S. 355-358 FROM THAT OF THE FIFTH CIRCUIT IN THE CASE OF COMMISSIONER v. FALCON CO., 127 Fed. (2d) 277, IN THAT THE FIFTH CIRCUIT HOLDS THE RULE ONLY APPLIES WHEN AN ISSUE OF FRAUD OR SUBTERFUGE HAS BEEN RAISED. IF THE CONSTRUCTION GIVEN BY THE FIFTH CIRCUIT IS CORRECT THEN THE JUDGMENT HERE SHOULD BE REVERSED.

We take the following quotations from the Court's opinion:

> "Appellant contends that under the State Law the license agreement was conclusive, but as stated above the State Law is not controlling. Appellant further contends that the conclusions of the Court below were erroneous, and argues that the agreements between him and the women definitely fixed their relationship as that of licensor and licensee, and that the other evidence regarding his 'control' over the women was as consistent with a 'license' as it was with an employer-employee relation." (R. 143.)

And again after quoting the common law and referring to the testimony, concludes,

> "Under ordinary standards an employer-employee relationship is indicated. It must be recognized, however, that all of these controls could be exercised through a license arrangement. If we are to consider the license agreement between the parties as conclusive on the origin and existence of the relationship, then it is clear that the arrangement between the parties was a license." (R. 144.)

The Circuit Court while recognizing that "all of these controls" could be exercised through the license agreement, gives as its sole answer to our contention that the license agreement is controlling, the rule laid down in *Griffith v. Commissioner,* 308 U. S. 355-358 from which the Circuit Court quotes as follows:

> "* * * Legislative words are not inert, and derive vitality from the obvious purposes at which they are aimed * * * taxes cannot be escaped 'by anticipatory arrangements and contracts however skilfully devised * * * by which the fruits are attributed to a different tree from that on which they grew.' Lucas v. Earl, 281 U. S. 111, 115 * * *" (R. 144.)

This case, however, can have no application here for the reason that it is based upon fraud. That the arrangement entered into between the parties was for the purpose of evading the income tax in question. That was one of the issues in the case. The Fifth Circuit in *Commissioner v. Falcon,* 127 Fed. (2d) 277, after referring to the *Griffith* and like cases said:

> "Here the record shows no fraud, sham, or subterfuge, or use of mere form to hide the substance of the real transaction."

Judge Major, in his dissenting opinion in *Campana Corporation v. Harrison,* 114 Fed. (2d) 400, 412 (Seventh Circuit) said,

> "It must not be overlooked that the plaintiff is not charged with formulating a scheme or device with the purpose of evading taxation. Cases such as Griffith v. Commissioner, 308 U. S. 35, and Higgins v. Smith, 308 U. S. 473, have no application".

It is obvious that the construction of the *Griffith* case given by the Ninth Circuit is contrary to that of the Fifth Circuit. It would seem that the construction of the Fifth Circuit is most logical. A trial Court can not arbitrarily set aside a written agreement, even though it may have the result of avoiding a tax unless fraud or a subterfuge is found. But fraud or subterfuge must be made an issue in the case in order to set it aside. No issue of fraud or subterfuge was raised in this case. The rule in the *Griffith* case should be limited to those cases involving fraud or subterfuge. If this be not done, then right to contract in employment matters has certainly been infringed upon where a taxing agency becomes involved. A contract creating an independent contractor in those instances would not be of any avail according to *Reeves v. Howard etc.,* 33 Fed. Supp. 90. The right to contract is still sacred and applies to employment contracts. See also *Gregory v. Helvering,* 293 U. S. 465, 79 L. Ed. 596. If we assume that the rule announced by the Fifth Circuit is correct, then the judgment should be reversed.

(2) THE CIRCUIT COURT ERRED IN HOLDING THAT THE STATE LAW WAS NOT CONTROLLING SINCE IT HELD THAT THE RELATIONSHIP OF EMPLOYER AND EMPLOYEE SHOULD BE ESTABLISHED UNDER THE COMMON LAW WHILE WE FIND THERE IS LITTLE IF ANY DIFFERENCE BETWEEN THE COMMON LAW AND THE STATE LAW, AND FURTHER THE CASE OF CHILDERS v. COMMISSIONER, SUPRA, HELD THAT THE CALIFORNIA LAW SHOULD BE APPLIED WHERE THE SAME ISSUE WAS RAISED BETWEEN CALIFORNIA CITIZENS.

The basic reason given by the Circuit Court of Appeals for not applying the standard fixed by the California law was that there is a difference between the Federal law and the State law as to the elements going to establish the employer-employee relationship. The Circuit Court readily admits that if the State law was applied, the judgment should have been reversed. It held, however, that the "State law is not controlling". The question that arises therefore is, does the State law differ from the Federal law in this particular.

The fact that a tax law is involved should not affect the situation. According to the Circuit Court opinion, apparently it does not because it held in *Anglim v. Empire Star Mines Co.*, 129 F. (2d) 914-917, that the regulation established for use in connection with the Social Security Act does no more than reiterate the familiar principles of common law. Obviously, the standard to determine the employer-employee relationship is laid down by the common law. The Circuit Court quotes from 35 Am. Jur. 445, Sec. 3, for the purpose of showing the elements required at common law to establish the relationship of master and servant. When you compare these elements with the California law, you will find little, if any difference.

However the Circuit Court of Appeals (Ninth Circuit) in the case of *Childers v. Commissioner,* 80 Fed. (2d) 27-30 where the employer-employee relationship was under consideration in connection wtih the Federal Income law, applied the California law in determining whether that relationship existed. It quoted approvingly from the following cases:

Green v. Soule, 145 Cal. 96-99;

Western Indemnity Co. v. Pillsbury, 172 Cal. 807-811;

Fidelity etc. Co. v. Industrial Accident Commission, 191 Cal. 404, 407.

If the California law was applied to the facts and circumstances found in the *Childers* case, then why should not the same standards be applied to the case at bar? In principle there is no distinction between the *Childers* case and the case at bar. Taxing acts and California citizens were involved in both cases.

According to the Circuit Court, the standard for determining the existence of the relationship of employer and employee is fixed by the principles of common law and not by the taxing act or regulations promulgated. If we are to be guided by the *Childers* case, then it is obvious that the Circuit Court erred in not applying the same principles to the case at bar.

With all due deference to the Circuit Court of Appeals of its discussion regarding "a nationwide scheme of taxation" we say that such discussion is beside any issue raised in this case. The main issue in the case at bar was whether the relation of employer and employee existed. If this is to be determined according to the standard of the common law then question

naturally follows, was there any difference between the State law and the Federal law. If the standard fixed by the common law was substantially the same as fixed by the State law, then the statement of the Circuit Court that the "State law is not controlling" cannot be sustained. The *Childers* case supra has fixed the standard by which the relationship in this case should have been established.

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(3) SINCE THIS LICENSE AGREEMENT WAS MADE BETWEEN CITIZENS OF CALIFORNIA AND IN THE STATE OF CALIFORNIA, IT SHOULD HAVE BEEN CONSTRUED UNDER THE LAWS OF THE STATE OF CALIFORNIA AND AS THUS CONSTRUED, IT WAS CONCLUSIVE ON THE ORIGIN AND EXISTENCE OF THE RELATIONSHIP BETWEEN APPELLANT AND SAID WOMEN.

A contract should be construed under the laws of the State in which the same is made.

Metropolis v. Kennedy, 84 U. S. 19;
George v. Tait, 102 U. S. 564;
Lewis v. Tollurido, 270 Fed. 590;
Missouri v. Holt, 293 Fed. 155;
Russell v. Young, 94 Fed. 45, 36 C.C.A. 71;
Philadelphia v. Trimble, 77 U. S. 367, 10 Wall. 367, 19 L. Ed. 948;
Paige v. Banlos, 80 U. S. 608, 13 Wall. 608, 20 L. Ed. 709.

The law of California in regard to the construction of contracts is found in the following sections of the Civil Code:

1625, 1636, 1637, 1638, 1639, 1641, 1643. Also Sec. 1856, Code of Civil Procedure and 6 Cal. Jur., Sec. 167.

According to the law of California where the contract is definite and certain, oral evidence is not admissible for the purpose of changing the intent of the parties as expressed in the writing. In other words, the intentions of the parties is to be determined from the instrument itself if it is certain and definite.

The Circuit Court, as did the trial Court, entirely ignored the written license notwithstanding the fact that it was definite and certain and on its face showed the relationship to be that of licensor or licensee. It did so without any issue being raised that the instrument was procured through fraud or was for the purpose of perpetrating a subterfuge. It is apparent that the Circuit Court erroneously concluded that where a taxing agency is involved that it is not bound by agreements made between parties for the purpose of establishing an employment relationship between them.

CONCLUSION.

There now exists a difference between the Circuit Courts of Appeals as to what extent the rule laid down in the case of *Griffith v. Commissioner,* supra, should apply. This difference should be settled.

It should be definitely established that the State law should be the guide in establishing the employer-employee relationship, particularly where the State law and common law are the same.

The Circuit Court upheld the trial Court in avoiding the written license involved simply because a tax-

ing agency was involved. Since there was no issue of fraud or subterfuge, it violated appellant's right to contract. It should have held that a written contract cannot be arbitrarily set aside, unless one of the those issues so justify.

This Court should review the decision of the Circuit Court of Appeals and finally reverse it.

Dated, Sacramento, California,
June 28, 1943.

Respectfully submitted,
HORACE B. WULFF,
Counsel for Petitioner.

R. H. SCHWAB,
Of Counsel.